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Proposed commentary on article 26

Proposed commentary on paragraphs 4 to 7 and the inventory of exchange mechanisms, prepared by the Interior Coordinator of the Subcommittee on Exchange of Information*

Summary

The proposed commentary on article 26 (proposed 2007) of the United Nations Model Double Taxation Convention between Developed and Developing Countries, paragraphs 4 to 7, and the inventory of exchange mechanisms are set out below. The proposed commentary discusses the removal of various limitations on an exchange of information. Paragraph 4 deals with the elimination of the rule allowing a Contracting State to avoid its obligation to provide information based on the fact that it has no domestic interest in the matter. Paragraph 5 requires a Contracting State to provide requested information notwithstanding domestic secrecy laws, including laws relating to information held by banks and fiduciaries. Paragraph 6 clarifies that a Contracting State is entitled to requested information whether or not criminal conduct is involved. Paragraph 7 authorizes the competent authorities to act in accordance with the obligations assumed by a Contracting State under paragraph 1.

The general considerations and proposed commentary on article 28 (proposed 2007), paragraphs 1 to 3, is contained in document E/C.18/2007/10.

* The present note has not yet been acted upon by the full Subcommittee. All comments received from members of the Subcommittee are reflected in the document. The views and opinions expressed are those of the authors and do not necessarily represent those of the United Nations.

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* See E/C.18/2007/10.

Commentary on paragraphs 4-7 of article 26 (proposed 2007)

Paragraph 4
Removal of domestic tax interest requirement

23. Paragraph 4 was added to the United Nations Model Convention in 2007. It is taken directly from the comparable provision added to the OECD Model Convention in 2005. As a result, the OECD commentary to paragraph 4 is fully applicable in interpreting paragraph 4 of article 26. The position taken in the OECD commentary is that the addition of this paragraph was intended to assist in the interpretation of article 26 and does not result in a substance change in the obligations implicit in the prior version of article 26.

23.1. According to paragraph 4, a requested State must use its information gathering measures to obtain requested information even though those measures are invoked solely to provide information to the other Contracting State. The term "information gathering measures" means laws and administrative or judicial procedures that enable a Contracting State to obtain and provide the requested information. That is, a requested State does not need to have a domestic tax interest in obtaining the requested information for the obligation to supply information under paragraph 1 to apply.

23.2. As stated in the second sentence of paragraph 4, the obligation imposed by that paragraph generally is subject to the limitations contained in paragraph 3. An exception applies, however, that prevents a requested State from avoiding an obligation to supply information due to domestic laws or practices that include a domestic tax interest requirement. Thus, a requested State cannot avoid an obligation to supply information on the ground that its domestic laws or practices only permit it to supply information in which it has an interest for its own tax purposes.

23.3. For many countries, the combination of paragraph 4 and their domestic law provides a sufficient basis for using their information gathering measures to obtain the requested information even in the absence of a domestic tax interest in the information. Other countries, however, may wish to clarify expressly in the convention that Contracting States must ensure that their competent authorities have the necessary powers to do so. Contracting States wishing to clarify this point may replace paragraph 4 with the following text:

> "4. In order to effectuate the exchange of information as provided in paragraph 1, each Contracting State shall take the necessary measures, including legislation, rule-making, or administrative arrangements, to ensure that its competent authority has sufficient powers under its domestic law to obtain information for the exchange of information, regardless of whether that Contracting State may need such information for its own tax purposes."

Paragraph 5
Secrecy limitations

24. Paragraph 4 was added to the United Nations Model Convention in 2007. It is taken directly from the comparable provision added to the OECD Model Convention in 2005. As a result, the OECD commentary to paragraph 5 is fully applicable in interpreting paragraph 5 of article 26. The discussion below of secrecy limitations

draws heavily from the OECD commentary. The position taken in the OECD commentary is that the addition of this paragraph was intended to assist in the interpretation of article 26 and does not result in a substance change in the obligations implicit in the prior version of article 26.

24.1. Paragraph 1 imposes a positive obligation on a Contracting State to exchange all types of information. Paragraph 5 is intended to ensure that the limitations of paragraph 3 cannot be used to prevent the exchange of information held by banks, other financial institutions, nominees, agents and fiduciaries, as well as ownership information.

24.2. Paragraph 5 states that a requested State shall not decline to supply information to a requesting State solely because the information requested is held by a bank or other financial institution. Thus, paragraph 5 overrides paragraph 3 to the extent that paragraph 3 would otherwise permit a requested Contracting State to decline to supply information on grounds of domestic bank secrecy laws. Access to information held by banks or other financial institutions may be by direct means or indirectly through a judicial or administrative process. The procedure for indirect access should not be so burdensome and time-consuming as to act as an impediment to access to bank information.

24.3. Paragraph 5 also provides that a Contracting State shall not decline to supply information solely because the information is held by persons acting in an agency or fiduciary capacity. For instance, if a Contracting State has a law under which all information held by a fiduciary is treated as a "professional secret" merely because it was held by a fiduciary, such State could not use such law as a basis for declining to provide the information held by the fiduciary to the other Contracting State. A person acts in a "fiduciary capacity" when the business which the person transacts, or the money or property which the person handles, is not its own or for its own benefit but is held for the benefit of another person and when the fiduciary stands in a relationship to that other person implying and necessitating confidence and trust on the one part and good faith on the other part. A trustee is a common example of a person acting in a fiduciary capacity. The term "agency" is very broad and includes all forms of corporate service providers (e.g., company formation agents, trust companies, registered agents, lawyers).

24.4. Paragraph 5 states that a Contracting State shall not decline to supply information solely because the requested information relates to an ownership interest in a person, including companies and partnerships, foundations or similar organizational structures. Information requests cannot be declined merely because domestic laws or practices may treat ownership information as a trade or other secret.

24.5. Although paragraph 5 limits the ability of a requested State to rely on paragraph 3 to refuse to supply information held by a bank, financial institution, a person acting in an agency or fiduciary capacity or to refuse to supply information relating to ownership interests, that paragraph does not eliminate all protection under paragraph 3. The requested State may continue to refuse to supply such information if that refusal is based on substantial reasons unrelated to the status of the holder of the requested information as a bank, financial institution, agent, fiduciary or nominee, or to the fact that the information relates to ownership interests.

24.6. A requested State is not necessarily prevented by paragraph 5 from declining under paragraph 3 (b) to supply information constituting a confidential communication between an attorney, solicitor, or other admitted legal representative and his client even if that person is acting in an agency capacity. To qualify for protection under paragraph 3 (b), however, a requested State must demonstrate that the communication between the attorney, solicitor, or other admitted legal representative and his client meets all the requirements of that paragraph, including that the communication is protected from disclosure under domestic law, that the refusal is unrelated to the status of the legal representative as an agent, fiduciary, or nominee, that any documents at issue were not delivered to the legal representative to avoid disclosure, and that non-disclosure would not frustrate an effective exchange of information.

24.7. Contracting States wishing to refer expressly to the protection afforded to confidential communications between a client and an attorney, solicitor or other admitted legal representative may do so by adding the following text at the end of paragraph 5:

> "Nothing in the above sentence shall prevent a Contracting State from declining to obtain or provide information which would reveal confidential communications between a client and an attorney, solicitor or other admitted legal representative where such communications are protected from disclosure under paragraph 3 (b) and when the claim for protection under that paragraph is unrelated to the status of the legal representative as an agent, fiduciary, or nominee."

25. The following examples illustrate the application of paragraph 5:

(a) Company X owns a majority of the stock in a subsidiary company Y, and both companies are incorporated under the laws of State A. State B is conducting a tax examination of business operations of company Y in State B. In the course of this examination the question of both direct and indirect ownership in company Y becomes relevant, and State B makes a request to State A for ownership information of any person in company Y's chain of ownership. In its reply, State A should provide to State B ownership information for both company X and company Y.

(b) An individual subject to tax in State A maintains a bank account with Bank B in State B. State A is examining the income tax return of the individual and makes a request to State B for all bank account income and asset information held by Bank B in order to determine whether there were deposits of untaxed earned income. State B should provide the requested bank information to State A.

(c) Bank A in State A is suspected of entering into secret letters of agreement with some of its depositors that direct the bank to pay interest earned by those depositors to an unrelated offshore bank. State B requests that State A provide it with copies of those secret letters of agreement. Bank A asserts that the letters of agreement are legal documents protected from disclosure under the lawyer-client privilege. State A should provide the requested documents.

Paragraph 6
Dual criminality

26. The United Nations Model Convention does not require the existence of criminal activity in either of the Contracting States for the obligation to exchange information to arise. Paragraph 6 is included in the text of article 26 primarily to deal with those limited number of treaties where criminal activity in the requested State is required under the terms of the treaty or under the domestic law of a Contracting State. It is also included, as a cautionary measure, to ensure that a requested State cannot use the absence of criminal activity in one or the other State to avoid its obligation to exchange information under article 26. Some countries may conclude that the inclusion of paragraph 6 is unnecessary and should be omitted.

Paragraph 7

27. The first sentence of paragraph 7 was taken, with minor changes, from the last sentence of paragraph 1 of the Model Convention before its amendment in 2007. The remaining two sentences were added in 2007. Paragraph 7 specifically grants to the competent authorities the authority to establish procedures for an effective exchange of information. The OECD Model Convention does not contain paragraph 7 or an equivalent. The position taken in the OECD commentary is that this authority is implicit in article 26.

27.1. The rule laid down in paragraph 7 allows information to be exchanged "on a routine basis or on request with reference to particular cases, or otherwise". "Or otherwise" would include spontaneous exchanges of information coming into the possession of one Contracting State and provided to the other Contracting State without request and outside the established programme for routine exchanges.

27.2. To achieve an effective exchange of information, the competent authorities of the Contracting States must work together to establish procedures for the exchange of information, including routine exchanges, typically in electronic form. Paragraph 7 not only authorizes the competent authorities to make such arrangements but also gives them a mandate to do so.

27.3. Some members of the Committee of Experts on International Cooperation in Tax Matters have expressed a concern that information requests from a developed country to a developing country could place excessive burdens on the tax department in the developing country. That concern might be alleviated by making the requesting State responsible for extraordinary costs associated with a request for information. In this context, the question of whether a cost of obtaining requested information is extraordinary would be determined not by reference to some absolute amount but by reference to the cost relative to the overall budget of the tax department being asked to provide information. For example, a relative small absolute cost might be extraordinary for a tax department with very limited resources, whereas even a large absolute cost might not be extraordinary for a well-funded department.

27.4. Countries concerned about imposing substantial costs on developing countries might include the following language at the end of paragraph 7:

> "Extraordinary costs incurred in providing information shall be borne by the Contracting Party which requests the information. The competent authorities

of the Contracting Parties shall consult with each other in advance if the costs of providing information with respect to a specific request are expected to be extraordinary."

Inventory of exchange mechanisms

1. Routine transmittal of information

28. A method of exchange of information is that of the routine or automatic flow of information from one treaty country to another. The term "transmitting country" refers to the country transmitting information, and the term "receiving country" refers to the country receiving information. The following are various aspects that the competent authorities should focus on in developing a structure for such routine exchange. In considering routine exchanges of information, it should be recognized that some countries not desiring to receive such information in a routine fashion (or unable to receive it routinely because the transmitting countries do not routinely collect such information) may desire to obtain information of this type under a specific request. Hence, in these situations, items mentioned in the present section should be considered as available for coverage under section 2 below, entitled "Transmittal on specific request".

Items covered

29. *Regular sources of income*. The items covered under a routine transmittal or exchange of information may extend to regular sources of income flowing between countries, such as dividends, interest, compensation (including wages, salaries, fees and commissions), royalties, rents and other possible items whose regular flow between the two countries is significant. It should be recognized that at present a few countries are not in a position to supply routine information of this type because their tax collection procedures do not provide the needed data.

30. *Transactions involving taxpayer activity*. A routine exchange of information may cover certain significant transactions involving taxpayer activity:

(a) Transactions relevant to the treaty itself:

(i) Claims for refund of transmitting country tax made by residents of receiving country;

(ii) Claims for exemption or particular relief from transmitting country tax made by residents of receiving country;

(b) Transactions relevant to special aspects of the legislation of the transmitting country: items of income derived by residents of the receiving country that receive exemption or partial relief under special provisions of the national law of the transmitting country;

(c) Transactions relating to activities in the transmitting country of residents of the receiving country:

(i) Opening and closing by receiving country residents of a branch, office etc. in the transmitting country;

(ii) Creation or termination by receiving country residents of a corporation in the transmitting country;

(iii) Creation or termination by receiving country residents of a trust in the transmitting country;

(iv) Opening and closing by receiving country residents of bank accounts in the transmitting country;

(v) Property in the transmitting country acquired by residents of the receiving country by inheritance, bequest or gift;

(vi) Ancillary probate proceedings in the transmitting country concerning receiving country residents;

(d) General information:

(i) Tax laws, administrative procedures etc. of the transmitting country;

(ii) Changes in regular sources of income flowing between countries, especially as they affect the treaty, including administrative interpretations of and court decisions on treaty provisions and administrative practices or developments affecting application of the treaty;

(iii) Activities that affect or distort application of the treaty, including new patterns or techniques of evasion or avoidance used by residents of the transmitting or receiving country;

(iv) Activities that have repercussions regarding the tax system of the receiving country, including new patterns or techniques of evasion or avoidance used by residents of either country that significantly affect the receiving country's tax system.

General operational aspects to be considered

31. The competent authorities should consider various factors that may have a bearing on the operational character of the routine exchange, including its effectiveness. For example:

(a) Countries that are more interested in receiving information on a specific request basis than on a routine basis, in their consideration of the specific request area, should keep in mind items mentioned in this inventory under the heading of routine information;

(b) A minimum floor amount may be fixed to limit minor data;

(c) The routine source of income items may be rotated from year to year, for example, dividends only in one year, interest in another etc.;

(d) The information to be exchanged routinely need not be reciprocal in all items. Country A may be interested in receiving information on some items but not others; the preferences of country B may extend to different items; it is not necessary for either country to receive items in which it is not interested, nor should either country refuse to transmit information on certain items simply because it is not interested in receiving information on those items;

(e) While the information to be exchanged on income items may not always be significant in itself as regards the income flows escaping tax, the routine exchange may provide indications respecting the degree to which the capital or other assets producing the income flows are escaping tax;

(f) Whether the information on items of income should cover the payee only or also the payer is a further point to be taken into account;

(g) Another factor to be considered is whether the information should cover only residents of the receiving country or also those domiciled therein or citizens thereof, or be limited to any of these categories;

(h) The degree of detail involved in the reporting, e.g., name of taxpayer or recipient, profession, address, etc., may need to be taken into account;

(i) The form and the language in which the information should be provided is a further point to be considered.

Factors to be considered by the transmitting country

32. The transmitting country may wish to give consideration to factors affecting its ability to fulfil the requirements of a routine exchange of information. Such a consideration would presumably lead to a more careful selection of the information to be routinely exchanged rather than to a decision not to exchange information that could be of practical use.

33. Among the factors to be considered are the administrative ability of the transmitting country to obtain the information involved. This, in turn, is governed by the general effectiveness of its administrative procedures, its use of withholding taxes, its use of information returns from payers or others, and the overall costs of obtaining the information involved.

Factors to be considered by receiving country

34. The receiving country may wish to give consideration to factors affecting its ability to use the information that could be received under a routine exchange of information, such as the administrative ability of the receiving country to use the information on a reasonably current basis and effectively to associate such information with its own taxpayers, either routinely or on a sufficient scale to justify the routine receipt of the information.

2. Transmittal on specific request

35. A method of exchange of information that is in current use is that of a request for specific information made by one treaty country to another. The specific information may relate to a particular taxpayer and certain facets of his situation, or to particular types of transactions or activities, or to information of a more general character. The following are various aspects of the question that the competent authorities should focus on in developing a structure for such exchange of information pursuant to specific requests.

Items covered

36. *Particular taxpayers*. The information that may be desired from a transmitting country with respect to a receiving country taxpayer is essentially open-ended and depends on the factors involved in the situation of the taxpayer under the tax system of the receiving country and the relationship of the taxpayer and his activities to the transmitting country. A specific enumeration in advance of the type of information that may be within the scope of an exchange pursuant to specific request does not

seem to be a fruitful or necessary task. The agreement to provide information pursuant to specific request may, thus, be open-ended as to the range, scope and type of information, subject to the overall constraints to be discussed herein.

37. The request for specific information may arise in a variety of ways. For example:

(a) Information needed to complete the determination of a taxpayer's liability in the receiving country when that liability depends on the taxpayer's worldwide income or assets; the nature of the stock ownership in the transmitting country of the receiving country corporation; the amount or type of expense incurred in the transmitting country; and the fiscal domicile of an individual or corporation;

(b) Information needed to determine the accuracy of a taxpayer's tax return to the tax administration of the receiving country or the accuracy of the claims or proof asserted by the taxpayer in defence of the tax return when the return is regarded as suspect or is under actual investigation;

(c) Information needed to determine the true liability of a taxpayer in the receiving country when it is suspected that his reported liability is wrong.

38. *Particular types of transactions or activities*. The exchange on specific request need not be confined to requests regarding particular taxpayers but may extend to requests for information on particular types of transactions or activities. For example:

(a) Information on price, cost, commission or other such patterns in the transmitting country necessary to enable the tax administration of the receiving country either to determine tax liability in a particular situation or to develop standards for investigation of its taxpayers in situations involving possible under-or over-invoicing of exported or imported goods, the payment of commissions on international transactions and the like;

(b) Information on the typical methods by which particular transactions or activities are customarily conducted in the transmitting country;

(c) Information on whether a particular type of activity is being carried on in the transmitting country that may have effects on taxpayers or tax liabilities in the receiving country.

39. *Economic relationships between the countries*. The specific request may extend to requests for information regarding certain economic relationships between the countries which may be useful to a country as a check on the effectiveness of its tax administration activities, for example:

(a) The volume of exports from the transmitting country to the receiving country;

(b) The volume of imports into the transmitting country from the receiving country;

(c) Names of banks dealing in the transmitting country with branches, subsidiaries, etc. of residents of the receiving country.

It should be noted that since items in this category, such as the volume of exports between the countries, are presumably not regarded as secret to the tax authorities in

the transmitting country, they may be disclosed generally in the receiving country, as provided in article 26.

Rules applicable to the specific request

40. The competent authorities should develop rules applicable to the transmission of specific requests by the receiving country and to the response by the transmitting country. These rules should be designed to facilitate a systematic operational procedure regarding such exchange that is both efficient and orderly. While the rules may be general in character in the sense that they set standards or guidelines governing the specific request procedures, the rules should also permit discussion between the competent authorities of special situations that either country believes require special handling. The rules should pertain to:

(a) The specificity of detail required in the request by the receiving country, the form of such request and the language of the request and reply;

(b) The extent to which the receiving country must pursue or exhaust its own administrative processes and possibilities before making a specific request; presumably the receiving country should make a bona fide effort to obtain the information for itself before resorting to the specific request procedure;

(c) The conditions affecting the nature and extent of the response by the transmitting country. This aspect should cover the ability of the transmitting country to provide documentary material when the receiving country needs material in that form for use in judicial or other proceedings, including the appropriate authentication of the documents.

3. Transmittal of information on discretionary initiative of transmitting country (spontaneous exchange)

41. The competent authorities should determine whether, in addition to the routine and specific request methods of exchange of information under which a transmitting country is automatically transmitting information or systematically responding to specific requests by the receiving country, they desire a transmittal of information on the discretionary initiative of the transmitting country itself. Such a transmittal could occur when, in the course of its own activities, the tax administration of the transmitting country obtains information that it considers would be of importance to the receiving country. The information may relate to facets of a particular taxpayer's situation and the relationship of that situation to his liability in the receiving country or to the liability of other taxpayers in the receiving country. Or the information may relate to a pattern of transactions or conduct by various taxpayers or groups of taxpayers occurring in either country that is likely to affect the tax liabilities or tax administration of the receiving country in relation either to its national laws or to the treaty provisions.

42. The competent authorities will have to determine, under the standards governing the exchange of information developed pursuant to the treaty, whether it is the duty of a transmitting country affirmatively to develop a procedure and guidelines governing when such information is to be transmitted, whether such transmittal is to be considered by the transmitting country but is fully discretionary, or whether such transmittal need not even be considered by the transmitting country. Even if it is agreed that it is the duty of the transmitting country to develop a system

for such transmittal, presumably the decision on when the conditions under that system have been met will rest on the discretionary judgement of the latter country.

4. Use of information received

43. The competent authorities will have to decide on the permissible use of the information received. The decisions on this matter basically depend on the legal requirements set forth in article 26 itself. The extent of the use of information depends primarily on the requirements of national law regarding the disclosure of tax information or on other "security requirements" regarding tax information. This being so, it is possible that the extent of the disclosure or the restrictions on disclosure may vary between the two countries. However, such possible variance need not be regarded as inappropriate or as negating exchanges of information that would otherwise occur if the countries involved are satisfied with such a consequence under article 26 as adopted in their Convention.

Recipients of information received through exchange

44. The competent authorities will have to specify, either in detail or by reference to existing comparable rules in the receiving country, who the qualifying recipients of information in that country are. Under article 26, the information can be disclosed, for example:

(a) To administrators of the taxes covered in the Convention;

(b) To enforcement officials and prosecutors for such taxes;

(c) To administrative tribunals for such taxes;

(d) To judicial tribunals for such taxes;

(e) In public court proceedings or in judicial decisions where it may become available to the public if considered appropriate;

(f) To the competent authority of another country (see sect. 5 below, entitled "Consultation among several competent authorities").

The form in which information is provided

45. The permissible extent of the disclosure may affect the form in which the information is to be provided if it is to be useful to the receiving country. Thus, if the information may be used in judicial tribunals, and if, to be so used, it must be of a particular character or form, then the competent authorities will have to consider how to provide for a transmittal that meets this need (see also the comment on documents in para. 40 (c) above).

5. Consultation among several competent authorities

46. Countries may wish to give consideration to procedures developed by the competent authorities for consultations covering more than the two competent authorities under a particular treaty. Thus, if countries A, B and C are joined in a network of treaties, the competent authorities of A, B and C might desire to hold a joint consultation. A joint meeting could be desired whether or not all three countries are directly intertwined by their treaty network. For example, the joint meeting might be desirable where there are A-B, A-C and B-C treaties or where

there are A-B and B-C treaties but not an A-C treaty. Countries desiring to have their competent authorities engage in such consultations should provide the legal basis for the consultations by adding the necessary authority in their treaties. Some countries may feel that article 26 permits joint consultation where all three countries are directly linked by bilateral treaties. However, the guideline does not cover joint consultation where a link in the chain is not fully joined, as in the second situation described above. In such a case, it would be necessary to add a treaty provision allowing the competent authority of country B to provide information received from country A to the competent authority of country C. Such a treaty provision could include a safeguard that the competent authority of country A must consent to the action of the competent authority of country B. Presumably, it would so consent only where it was satisfied as to the provisions regarding protection of secrecy in the B-C treaty.

6. Overall factors

47. There are a variety of overall factors affecting the exchanges of information that the competent authorities will have to consider and decide upon, either as to their specific operational handling in the implementation of the exchange of information or as to their effect on the entire exchange process itself. Such overall factors include those set out below.

Factors affecting implementation of exchange of information

48. These include the following:

(a) The competent authorities should decide on the channels of communication for the different types of exchanges of information. One method of communication that may be provided for is to permit an official of one country to go in person to the other country to receive the information from the competent authority and discuss it so as to expedite the process of exchange of information;

(b) Some countries may have decided that it is useful and appropriate for a country to have representatives of its own tax administration stationed in the other treaty country. Such an arrangement would presumably rest on authority, treaty or agreements other than that in the article on exchange of information of the envisaged double taxation treaty (though, if national laws of both countries permit, this article would be treated as covering this topic), and the arrangement would determine the conditions governing the presence of such representatives and their duties. In this regard, it should be noted that it would not seem necessary that the process be reciprocal, so that it would be appropriate for country A to have its representatives in country B but not vice versa if country A considered the process to be useful and country B did not. If arrangements do exist for such representatives, then the competent authorities may want to coordinate with those representatives where such coordination would make the exchange of information process more effective and where such coordination is otherwise appropriate;

(c) Some countries may decide it is appropriate to have a tax official of one country participate directly with tax officials of the other country in a joint or "team" investigation of a particular taxpayer or activity. The existence of the arrangement for most countries would presumably rest on authority, treaty or agreements other than that in the envisaged treaty article on exchange of information, although, if national laws of both countries permit, this article could be

treated by the countries as authorizing the competent authorities to sanction this arrangement. In either event, if the arrangement is made, it would be appropriate to extend to such an investigation the safeguards and procedures developed under the envisaged treaty article on exchange of information;

(d) The process of exchange of information should be developed so that it has the needed relevance to the effective implementation of the substantive treaty provisions. Thus, treaty provisions regarding intercompany pricing and the allocation of income and expenses produce their own informational requirements for effective implementation. The exchange of information process should be responsive to those requirements;

(e) The substantive provisions of the treaty should take account of and be responsive to the exchange of information process. Thus, if there is an adequate informational base for the exchange of information process to support allowing one country to deduct expenses incurred in another country, then the treaty should be developed on the basis of the substantive appropriateness of such deduction;

(f) The competent authorities will have to determine to what extent there should be cost sharing or cost reimbursement with respect to the process of exchange of information.

Factors affecting the structure of the exchange of information process

49. These include the following:

(a) It should be recognized that the arrangements regarding exchange of information worked out by country A with country B need not parallel those worked out between country A and country C or between country B and country C. The arrangements should in the first instance be responsive to the needs of the two countries directly involved and need not be fully parallel in every case just for the sake of formal uniformity. However, it should be observed that prevention of international tax evasion and avoidance will often require international cooperation of tax authorities in a number of countries. As a consequence, some countries may consider it appropriate to devise procedures and treaty provisions that are sufficiently flexible to enable them to extend their cooperation to multi-country consultation and exchange arrangements;

(b) The competent authorities will have to weigh the effect of a domestic legal restriction on obtaining information in a country that requests information from another country not under a similar domestic legal restriction. Thus, suppose country A requests information from country B, and the tax authorities in country B are able to go to their financial institutions to obtain such information, whereas the tax authorities in country A are generally not able to go to their own financial institutions to obtain information for tax purposes. How should the matter be regarded in country B? It should be noted that article 26 here permits country B to obtain the information from its financial institutions and transmit it to country A. Thus, country B is not barred by its domestic laws regarding tax secrecy if it decides to obtain and transmit the information. Thus, it becomes a matter of discretion in country B as to whether it should respond, and may perhaps become a matter for negotiation between the competent authorities. It should be noted that many countries in practice do respond in this situation and that such a course is indeed useful in achieving effective exchange of information to prevent tax avoidance.

However, it should also be noted that country A, being anxious to obtain information in such cases from other countries, should also recognize its responsibility to try to change its domestic laws to strengthen the domestic authority of its own tax administration and to enable it to respond to requests from other countries. It should be noted that countries that have entered into a tax convention that includes paragraph 5 of article 26 of the United Nations Model Convention are required to provide information to its treaty partner notwithstanding its domestic bank secrecy laws;

(c) In addition to situations involving the legal imbalance discussed above, the competent authorities will have to weigh the effects of a possible imbalance growing out of a divergence in other aspects of tax administration. Thus, if country A cannot respond as fully to a request as country B can because of practical problems of tax administration in country A, then might the level of the process of exchange of information be geared to the position of country A? Or, in general or in particular aspects, should country B be willing to respond to requests of country A even when country A would not be able to respond to requests of country B? This matter is similar to that discussed in the preceding paragraph, and a similar response should be noted;

(d) It should be noted that article 26 authorizes a transmitting country to use its administrative procedures solely to provide information to the requesting country, even when the person about whom information is sought is not involved in a tax proceeding in the transmitting country. Moreover, the transmitting country should, for the purpose of exchange of information, use its own administrative authority in the same way as if its own taxation were involved;

(e) The competent authorities will have to weigh the effect on the process of exchange of information of one country's belief that the tax system or tax administration of the other country, either in general or in particular situations, is discriminatory or confiscatory. It may be that further exploration of such a belief could lead to substantive provisions in the treaty or in national law that would eliminate the problems perceived by the first country and thereby facilitate a process of exchange of information. One possible example of this is the treatment of non-permanent residents;

(f) The competent authorities will have to weigh the effects that the process of exchange of information may have on the competitive position of taxpayers of the countries involved. Thus, if country A has a treaty with country B providing for exchange of information, country A will have to weigh the effect on the structure or process of that exchange of the fact that country C does not have a treaty with country B, so that firms of country C doing business in country B may be subject to a different tax posture in country B than firms of country A. Similarly, even if a treaty with an exchange of information article exists between countries C and B, if the tax administration of country A has more authority to obtain information (to be exchanged with country B) than does the tax administration of country C, or is otherwise more effective in its administration and, therefore, has more information, then a similar difference in tax posture may result. As a corollary, it seems clear that the adequate implementation of exchange of information provisions requires a universal effort of tax administrations to obtain and develop under national laws a capacity for securing information and a competence in utilizing information that is appropriate to a high level of efficient and equitable tax administration.

Periodic consultation and review

50. Since differences in interpretation and application, specific difficulties and unforeseen problems and situations are bound to arise, provision must be made for efficient and expeditious consultation between the competent authorities. Such consultation should extend both to particular situations and problems and to periodic review of the operations under the exchange of information provision. The periodic review should ensure that the process of exchange of information is working with the requisite promptness and efficiency, that it is meeting the basic requirements of treaty implementation, and that it is promoting adequate compliance with treaty provisions and the national laws of the two countries.